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No. -

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IN THE

SUPREME COURT OF THE UNITED STATES

October Term, 1988

THE NEMOURS FOUNDATION, GILBANE BUILDING COMPANY, AND THE AETNA CASUALTY & SURETY COMPANY,

Petitioners,

v.

PIERCE ASSOCIATES, INC. AND FEDERAL INSURANCE CO.,

Respondents.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

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QUESTIONS PRESENTED

1. Should a federal court of appeals accord deference to a federal district court's determination of the law of the state in which it sits, particularly where the appellate panel majority is composed of a newly-appointed appellate judge and a district judge sitting by designation, both from states other than the one whose law is being determined, and three experienced district court judges on three separate occasions had determined the law of their state?

2. Where the highest court of a state has not spoken, must a federal court sitting in diversity follow a dated lower state court decision in order to determine state substantive law or may it take into account developments in state law since the lower court decision, including analogous state supreme court rulings?

3. Is a federal court sitting in diversity required to apply state substantive law as declared by the highest court of a state?

PARTIES TO THE PROCEEDING

The named appellants/cross-appellees in the United States Court of Appeals for the Third Circuit, and the only respondents here, are Pierce Associates, Inc. and Federal Insurance Co. Pierce was the mechanical subcontractor for an addition to the A.I. duPont Institute, a children's hospital in Wilmington, Delaware. Federal was Pierce's surety on a performance bond.

The named appellees/cross-appellants in the court of appeals, and the only petitioners here, are The Nemours Foundation, Gilbane Building Company, and The Aetna Casualty & Surety Company. Nemours is a charitable foundation that owns and operates the A.I. duPont Institute. Gilbane was the general contractor for the addition to the hospital. Aetna was surety on Gilbane's performance bond.

TABLE OF CONTENTS

	Page
Questions Presented	i
Parties to the Proceeding	ii
Table of Authorities	v
Opinions Below	2
Jurisdiction	2
Statutory and Constitutional Provisions Involved	3
Statement of the Case	3
Reasons for Granting the Writ	6
I. CERTIORARI SHOULD BE GRANTED IN ORDER TO END THE CONFUSION IN THE COURTS OF APPEALS ABOUT THE WEIGHT TO BE GIVEN TO A DISTRICT COURT'S DETERMINATION OF THE LAW OF THE STATE IN WHICH IT SITS	7
II. CERTIORARI SHOULD BE GRANTED IN ORDER TO END THE CONFUSION IN THE FEDERAL COURTS SITTING IN DIVERSITY ABOUT HOW TO DETERMINE STATE LAW AS MANDATED BY *ERIE RAILROAD V. TOMPKINS*	11
A. This Case Evidences a Fundamental Confusion in the Federal Courts Regarding the Effect of Lower State Court Decisions on Federal Courts Sitting in Diversity	11
B. This Case Evidences a Fundamental Confusion in the Federal Courts Regarding Whether Decisions of a State's Highest Court Are Binding on Federal Courts Sitting in Diversity	17
Conclusion	21

TABLE OF CONTENTS—*(Continued)*

Page

Appendix (Separately Bound)

Court of Appeals Opinion A1

District Court Opinions

District Court Omnibus Order on Pending Motions, March 15, 1984 ..... A44

District Court Opinion and Order, March 25, 1985 ..... A50

District Court Oral Opinion and Order on Defendant's Motion for a Directed Verdict, August 18, 1986 ..... A74

Court of Appeals Judgment A80

Court of Appeals Order Denying Petition for Rehearing A82

TABLE OF AUTHORITIES

Cases Page

Agristor Leasing v. Saylor, 803 F.2d 1401 (6th Cir. 1986) 9

Allen v. A. G. Edwards & Sons, Inc., 606 F.2d 84 (5th Cir. 1979) 16

Aloe Coal Co. v. Clark Equipment Co., 816 F.2d 110 (3d Cir.), *cert. denied*, 108 S.Ct. 156 (1987) 13

Bernhardt v. Polygraphic Co. of America, 350 U.S. 198 (1956) 8, 19

Birmingham Fire Insurance Co. v. Winegardner & Hammons, Inc., 714 F.2d 548 (5th Cir. 1983) 16, 20

Blum v. Witco Chemical Corp., 829 F.2d 367 (3d Cir. 1987) 10

Bridgman v. Cornwell Quality Tools Co., 831 F.2d 174 (8th Cir. 1987) 9

Burrus v. Young, 808 F.2d 578 (7th Cir. 1986) 16

Camacho v. Civil Service Commission, 666 F.2d 1257 (9th Cir. 1982) 9

Ciccarelli v. Carey Canadian Mines, Ltd., 757 F.2d 548 (3d Cir. 1985) 17, 20

Ciociola v. Delaware Coca-Cola Bottling Co., 172 A.2d 252 (Del. 1961) 11, 12

Coleman v. Western Electric Co., 671 F.2d 980 (6th Cir. 1982) 17

Commissioner v. Estate of Bosch, 387 U.S. 456 (1967). 14, 15

Compagnie des Bauxites v. Insurance Co. of North America, 724 F.2d 369 (3d Cir. 1983) 10

Continental Grain Co. v. Martin, 536 F.2d 592 (5th Cir.), *cert. denied*, 429 U.S. 1024 (1976) 16

Crowell Corp. v. Topkis Construction Co., 280 A.2d 730 (Del. Super. 1971) 12

TABLE OF AUTHORITIES—*(Continued)*

Cases Page

Dale Baker Oldsmobile, Inc. v. Fiat Motors of North America, 794 F.2d 213 (6th Cir. 1986) 17

Delano v. Kitch, 663 F.2d 990 (10th Cir. 1981), *cert. denied*, 456 U.S. 946 (1982) 16

East River Steamship Corp. v. Transamerica Delaval, Inc., 476 U.S. 858 (1986) 13

Erie Railroad v. Tompkins, 304 U.S. 64 (1938) 6, 13, 14, 17, 20, 21

Farmer v. Travelers Indemnity Co., 539 F.2d 562 (5th Cir. 1976) 16

Fidelity Union Trust Co. v. Field, 311 U.S. 169 (1940) .. 14

Flintkote Co. v. Dravo Corp., 678 F.2d 942 (11th Cir. 1982) 16

Gaines v. Haughton, 645 F.2d 761 (9th Cir. 1981), *cert. denied*, 454 U.S. 1145 (1982) 9

General Electric Credit Corp. v. Ger-Beck Machine Co., 806 F.2d 1207 (3d Cir. 1986) 16

Harris v. Hercules, Inc., 455 F.2d 267 (8th Cir. 1972) ... 9

Hartzell v. United States, 539 F.2d 65 (10th Cir. 1976) .. 9

Harville v. Anchor-Wate Co., 663 F.2d 598 (5th Cir. 1981) 9

Hauser v. Public Service Co., 797 F.2d 876 (10th Cir. 1986) 9

Hill v. Bache Halsey Stuart Shields Inc., 790 F.2d 817 (10th Cir. 1986) 16

Hogue v. Pellerin Laundry Machinery Sales Co., 353 F.2d 772 (8th Cir. 1965) 9

In re Mitsura, Inc., 705 F.2d 1496 (9th Cir. 1983) 9

Jablonski by Pahls v. United States, 712 F.2d 391 (9th Cir. 1983) 9

Cases Page

King v. Order of United Commercial Travelers of America, 333 U.S. 153 (1948) 15

Kirby v. United States, 329 F.2d 735 (10th Cir. 1964) ... 9

Kochins v. Linden-Alimak, Inc., 799 F.2d 1128 (6th Cir. 1986) 16

Louisville & Jefferson County Metropolitan Sewer District v. Travelers Insurance Co., 753 F.2d 533 (6th Cir. 1985) 9

Martin v. Ryder Truck Rental, Inc., 353 A.2d 581 (Del. 1976) 11, 12

Mason v. American Emery Wheel Works, 241 F.2d 906 (1st Cir.), *cert. denied*, 355 U.S. 815 (1957) 20

Mathis v. Eli Lilly & Co., 719 F.2d 134 (6th Cir. 1983) .. 17

Matter of McLinn, 739 F.2d 1395 (9th Cir. 1984) (in banc) 9

McCoy v. Richards, 771 F.2d 1108 (7th Cir. 1985) 16

Meredith v. City of Winter Haven, 320 U.S. 228 (1943) . 19

Miller v. Fairchild Industries, Inc., 797 F.2d 727 (9th Cir. 1986) 16

Miller v. Premier Corp., 608 F.2d 973 (4th Cir. 1979) ... 20

Monte Carlo Shirt, Inc. v. Daewoo International (America) Corp., 707 F.2d 1054 (9th Cir. 1983) 9

Oliver B. Cannon & Sons, Inc. v. Dorr-Oliver Inc., 312 A.2d 322 (Del. Super. 1973) 13

Oliver B. Cannon & Son, Inc. v. Dorr-Oliver, Inc., 336 A.2d 211 (Del. 1975) 13, 17, 18

O'Neil v. Great Plains Women's Clinic, Inc., 759 F.2d 787 (10th Cir. 1985) 16

Provau v. State Farm Mutual Automobile Insurance Co., 772 F.2d 817 (11th Cir. 1985) 16

TABLE OF AUTHORITIES—*(Continued)*

Cases Page

Rhynes v. Branick Manufacturing Corp., 629 F.2d 409 (5th Cir. 1980) 20

Roginsky v. Richardson-Merrell, Inc., 378 F.2d 832 (2d Cir. 1967) 20

Royal Indemnity Co. v. Alexander Industries, Inc., 211 A.2d 919 (Del. 1965) 18

Rudd-Melikian, Inc. v. Merritt, 282 F.2d 924 (6th Cir. 1960) 9

Saludes v. Ramos, 744 F.2d 992 (3d Cir. 1984) 10

Santiago v. Johnson Machine & Press Corp., 834 F.2d 84 (3d Cir. 1987) 10, 14

Sarnoff v. American Home Products Corp., 798 F.2d 1075 (7th Cir. 1986) 17

Sears, Roebuck & Co. v. Jardel Co., 421 F.2d 1048 (3d Cir. 1970) 18

Seiler v. Levitz Furniture Co., 367 A.2d 999 (Del. 1976) 11, 12

Six Cos. v. Joint Highway District No. 13, 311 U.S. 180 (1940) 14

Stoner v. New York Life Insurance Co., 311 U.S. 464 (1940) 14

Studstill v. Borg Warner Leasing, 806 F.2d 1005 (11th Cir. 1986) 16

United States v. Hohri, 482 U.S. 64 (1987) 8

Weatherhead v. Globe International, Inc., 832 F.2d 1226 (10th Cir. 1987) 9

West v. American Telephone & Telegraph Co., 311 U.S. 223 (1940) 14

TABLE OF AUTHORITIES—*(Continued)*

Statutes Page

28 U.S.C. § 1254 (1) 3

28 U.S.C. § 1652 ..... 3, 13

Judicial Improvements and Access to Justice Act, Pub. L. No. 100-702, §§ 201 *et. seq.* (November 19, 1988) (amending 28 U.S.C. § 1332) 7

Other Authorities

Note, *Binding Effect of Intermediate State Court Decisions on Federal Courts*, 9 Geo. Wash. L. Rev. 458 (1941) 14

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PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

In the twenty-one years since this Court last considered the question of how federal courts sitting in diversity should determine state substantive law, the differences among the various courts of appeals have grown wider and wider with respect to the deference due determinations made by federal district judges sitting in the state whose law is being determined, by lower state courts of that state, and even, remarkably enough, by the highest court of the state. Those differences in the circuits are in part a result of language contained

in earlier opinions of this Court and in part an example of the centrifugal action of the courts of appeals over time. The effect, however, is that litigants can no longer ascertain with any assurance how state law will be determined and applied in diversity cases.

Here the court of appeals reversed uniform rulings of three experienced Delaware district judges, followed a 1971 lower state court decision called into question by more recent Delaware Supreme Court cases and rejected by the district judges, and then sought to distinguish and refused to follow more recent Delaware Supreme Court decisions which the district judges had all followed. Accordingly, this case presents the ideal vehicle to erase the uncertainty and eliminate the conflicts among the circuits because it presents clear questions of the deference due to the federal district court in Delaware, as well as to the Delaware state courts in determining Delaware law.

OPINIONS BELOW

The United States District Court for the District of Delaware rendered numerous unreported opinions in this case during the five years in which the parties were engaged in pretrial proceedings in that court, in addition to several reported opinions. The district court Omnibus Order on Pending Motions (A44-A49) is unreported. The district court opinion (A50-A73) granting in part and denying in part Nemours' motion to dismiss Pierce's and another subcontractor's counterclaim is reported at 606 F. Supp. 995. The district court Oral Opinion and Order on Defendant's Motion for a Directed Verdict (A74-A79) is unreported. Other district court opinions not relevant to the issues before the Court are reported at 568 F. Supp. 1085; 666 F. Supp. 649; and 632 F. Supp. 418. The opinion of the United States Court of Appeals for the Third Circuit (A1-A43) is reported at 865 F.2d 530.

JURISDICTION

The judgment of the court of appeals was entered on

December 29, 1988. The order denying rehearing and suggestion of rehearing in banc was entered on February 3, 1989. The jurisdiction of this Court is invoked pursuant to 28 U.S.C. § 1254(1).

STATUTORY AND CONSTITUTIONAL PROVISIONS INVOLVED

The Rules of Decision Act, 28 U.S.C. § 1652, provides:

> The laws of the several states, except where the Constitution or treaties of the United States or Acts of Congress otherwise require or provide, shall be regarded as rules of decision in civil actions in the courts of the United States, in cases where they apply.

STATEMENT OF THE CASE

In 1980, in order to construct a large addition to its children's hospital, Nemours entered into a general contract with Gilbane. As Nemours' managing contractor, Gilbane then entered into a number of subcontracts with various subcontractors, including a $36 million subcontract with Pierce for mechanical work. The Federal Insurance Company became surety on a performance bond, whose premium was paid by Nemours, naming Pierce as principal and Gilbane as obligee.

Disputes about performance under the general contract and subcontracts led to multiple lawsuits, later consolidated, in the District Court for the District of Delaware. Federal jurisdiction was based on diversity of citizenship. Included in these lawsuits were Nemours' claim for breach of contract against Gilbane based primarily on the acts and omissions of Pierce, as well as Nemours' direct claims against Pierce both as a third party beneficiary of the Gilbane/Pierce subcontract and for negligence.

District Judge James L. Latchum denied Pierce's motion to dismiss Nemours' claims against it, holding that under Delaware law both the third party beneficiary and negligence causes of action were legally sufficient (A44-A49). Judge Walter K. Stapleton, assigned when Judge Latchum took senior status, likewise recognized Nemours to be a third party beneficiary of the Gilbane/Pierce subcontract and held that, under Delaware law, negligence actions could be maintained for economic loss without privity (A72, A67).

In the midst of pretrial proceedings, at the urging of the district court, all thirteen parties engaged in an elaborate minitrial designed to bring about settlement. The result was that a multitude of claims were settled; eight parties were dismissed; and the remaining parties, Nemours, Aetna, Gilbane, Pierce, and Federal, were realigned by the district court.

To effect the settlement sought by the district court and relying on the rulings of the two Delaware federal district court judges, Nemours dismissed its breach of contract claim against Gilbane, leaving only its direct claims against Pierce. Thus, in March 1986, on the basis of the minitrial and the settlement, the case went to trial on Nemours' claims against Pierce and Federal; Gilbane's claims against Pierce and Federal; and Pierce's claims against Nemours and Gilbane. The trial lasted 79 days.

At the close of the evidence Pierce once again challenged the legal sufficiency of Nemours' third party beneficiary and negligence claims, either one of which would have supported the compensatory verdict in favor of Nemours and Gilbane. Judge Joseph J. Farnan, Jr., who had taken over the case when Judge Stapleton was appointed to the Court of Appeals for the Third Circuit, once again ruled that Nemours' direct actions against Pierce, both in contract and in tort, were properly brought under Delaware law (A75).

Thus, by the time the case went to the jury, *three* Dela-

ware district court judges had determined on *three* separate occasions that Delaware law would (1) recognize Nemours to be a third party beneficiary of the Gilbane/Pierce subcontract, and (2) permit recovery in tort for purely economic loss, without privity of contract.

The jury found in favor of Nemours and Gilbane on every one of their claims against Pierce and Federal and against Pierce and Federal on every one of their claims against Nemours and Gilbane. The jury found that Pierce had breached its contract, was grossly negligent, and had acted in an oppressive, malicious, wanton and willful manner, with a callous indifference for the harm it had caused. Judgment was entered awarding a total of over $29 million to Nemours and Gilbane, including approximately $2 million in punitive damages.

On appeal Pierce and Federal did not challenge the jury's findings in any regard and specifically did not challenge the findings with regard to their gross misconduct or the sufficiency of the evidence to support the amount of damages. Nonetheless, the panel majority of the court of appeals—a newly-appointed court of appeals judge from Pennsylvania and a district court judge from New Jersey sitting by designation—reversed, holding that the three Delaware district court judges each had erred in their state law determinations and that neither the third party beneficiary claim nor the negligence claim should have been presented to the jury (A18, A23). The dissenting judge would have affirmed the district court's ruling on the third party beneficiary issue (A41).

Thus, solely because Nemours tried its case directly against Pierce, rather than through Gilbane, the majority saddled a charitable institution with more than $24 million in damages that indisputably were the result of Pierce's wrongdoing. Moreover, in substituting its own view of state law for that of the Delaware district judges, the panel majority on one issue elevated the holding of an outdated lower state court

decision over subsequent decisions of the highest court of the state that evidenced a different view; and, on another issue, utterly disregarded controlling precedent by the highest court of the state.[1]

REASONS FOR GRANTING THE WRIT

In the fifty-one years of jurisprudence since *Erie Railroad v. Tompkins*, 304 U.S. 64 (1938), the task of applying state law in diversity cases has led to a myriad of problems for the federal courts, many of which this Court has resolved over time. However, the Court has been virtually silent on the issue of the extent to which a court of appeals should defer to a state law determination made by the federal district court sitting in the state whose law must be determined when the state's highest court has not spoken. The Court's lack of guidance on this important issue has led to widely differing approaches by the circuits.

Moreover, while there was extensive Supreme Court discussion regarding the effect of lower state court decisions and the binding effect of decisions of the highest court of a state during the 1940's, the only substantive consideration since that time has been sporadic and has called in question the earlier decisions to some degree. The lack of guidance in these areas has created confusion among and within the circuits, a confusion that created the tragic results in this case.

As the next sections will demonstrate, this case is a striking example of how a court of appeals can go astray in ascertaining or predicting state law, and why the federal

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1. On April 21, 1989, counsel for Pierce opposed an effort to have the U.S. district court in Delaware certify to the highest state court of Delaware the same two state law questions present in this case. Transcript of argument before Judge Farnan, dated April 21, 1989, in *Nemours v. Manganaro Corp.*, C.A. 89-138. On May 5, 1989 the district court certified the question to the Delaware Supreme Court for resolution.

courts are in urgent need of current guidance from this Court in this area.[2]

I. CERTIORARI SHOULD BE GRANTED IN ORDER TO END THE CONFUSION IN THE COURTS OF APPEALS ABOUT THE WEIGHT TO BE GIVEN TO A DISTRICT COURT'S DETERMINATION OF THE LAW OF THE STATE IN WHICH IT SITS.

The panel majority gave virtually *no* weight to the Delaware state law determinations that were made independently and on three separate occasions by three Delaware federal district court judges sitting in Delaware. Instead, the majority, consisting of a newly-appointed appellate court judge from Pennsylvania and a district court judge from New Jersey sitting by designation, simply made its own determinations of Delaware law.

On the third party beneficiary issue, the majority failed even to mention the fact that three Delaware district court judges on three occasions had recognized Nemours as a third party beneficiary of the Gilbane/Pierce subcontract in accordance with Delaware law. On the negligence issue, the court of appeals did note that the Delaware district court, relying on a series of decisions of Delaware's highest court, had held that the highest court of Delaware would permit recovery in tort for economic loss absent privity of contract. However, the court of appeals chose to reject the district court's state law determination, relying instead on an outdated lower state court case and on two inapplicable federal cases.

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2. This need becomes particularly acute in view of Congress' recent reaffirmation of diversity jurisdiction. Judicial Improvements and Access to Justice Act, Pub. L. No. 100-702, §§ 201 *et. seq.* (November 19, 1988) (amending 28 U.S.C. § 1332). In 1987, in 28% of all cases filed in federal court, jurisdiction was founded on diversity of citizenship. This constituted a 5.3% increase from 1986, even though fewer cases overall were filed in federal court in 1987 than in 1986. *1987 Annual Report of the Director of the Administrative Office of the United States Courts*, 8.

This Court has never directly ruled on the issue of the weight a court of appeals should give state law determinations of a federal district court in the state in which it sits. On several occasions, however, the Court has suggested that a district court's determination of the law of its state should be reviewed with "great deference." *United States v. Hohri*, 482 U.S. 64, 74 n.6 (1987); *see also Bernhardt v. Polygraphic Co. of America*, 350 U.S. 198, 204 (1956) "([s]ince the federal judge making those findings [of Vermont law] is from the Vermont bar, we give special weight to his statement of what the Vermont law is").

The court of appeals' utter refusal to accord any deference whatsoever to the district court's state law determinations not only conflicts with this Court's teachings in *Hohri* and *Bernhardt*, but also creates the untenable result that a district court judge from one state, sitting by designation on the appellate court and joined by a newly-appointed federal appellate judge from another state, is able to reverse the considered determinations of the law of a third state made by three experienced district court judges sitting in that third state.[3] Moreover, the court of appeals' failure to give any weight to the state law determinations of the district court conflicts with the majority of the circuits that have considered the question and reveals a fundamental tension in the courts of appeals about the magnitude of deference to be accorded a district court's state law determination.

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3. The district court judges in this case, Judge Latchum, Judge Stapleton, and Judge Farnan, have among them over forty years experience as practicing attorneys in Delaware, and over forty years experience as district court judges in Delaware. Judge Latchum served as Chief Judge of the Delaware district court from 1968 through 1983. Judge Stapleton was Chief Judge of the Delaware district court from 1983 until 1985, when he was appointed to the United States Court of Appeals for the Third Circuit. Judge Farnan was the United States Attorney in Delaware from 1981 until 1985, when he was appointed to the United States District Court for the District of Delaware.

Because the determination of state law where the highest court in the state has not spoken is, in a larger sense, a factual determination, many courts of appeals treat the state law determinations of district courts as binding unless clearly erroneous. This approach appears particularly prevalent in the Fifth, Eighth, and Tenth Circuits. *See, e.g., Weatherhead v. Globe International, Inc.*, 832 F.2d 1226, 1228 (10th Cir. 1987); *Bridgman v. Cornwell Quality Tools Co.*, 831 F.2d 174, 175 (8th Cir. 1987); *Hauser v. Public Service Co.*, 797 F.2d 876, 878 (10th Cir. 1986); *Harville v. Anchor-Wate Co.*, 663 F.2d 598, 602 (5th Cir. 1981); *Hartzell v. United States*, 539 F.2d 65, 68 (10th Cir. 1976); *Harris v. Hercules, Inc.*, 455 F.2d 267, 269 (8th Cir. 1972); *Hogue v. Pellerin Laundry Machinery Sales Co.*, 353 F.2d 772, 776 (8th Cir. 1965); *Kirby v. United States*, 329 F.2d 735, 737 (10th Cir. 1964).[4]

The court of appeals here, on the other hand, applied a plenary standard of review to the district court's state law determination, and rejected the concept of deference altogether. This approach also has been followed in the Ninth Circuit, for example, in *Matter of McLinn*, 739 F.2d 1395 (9th Cir. 1984) (in banc), where the court flatly rejected the concept of deference to a district court's state law determination, holding that "our appellate review of conclusions of state law should be under the same independent de novo standard as conclusions of federal law." *Id.* at 1403.[5]

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4. Other courts of appeals, while according considerable deference to district court determinations of state law, apply a standard of review slightly different from the clearly erroneous standard. The Sixth Circuit, for example, has long followed the view that "if a federal district judge has reached a permissible conclusion upon a question of local law, the Court of Appeals should not reverse, even though it may think the law should be otherwise." *Rudd-Melikian, Inc. v. Merritt*, 282 F.2d 924, 929 (6th Cir. 1960); *see also Agristor Leasing v. Saylor*, 803 F.2d 1401, 1407 (6th Cir. 1986); *Louisville & Jefferson County Metropolitan Sewer Dist. v. Travelers Insurance Co.*, 753 F.2d 533, 540 (6th Cir. 1985).

5. *McLinn* overruled numerous Ninth Circuit opinions that had applied a deferential standard of review to a district court's state law determi-

The fact that a court of appeals applies a plenary standard of review does not necessarily mean that it will not show deference to district court determinations of state law. Thus, the Third Circuit has consistently applied a plenary standard of review to district court determinations of state law, as it did here, *see, e.g., Santiago v. Johnson Machine & Press Corp.*, 834 F.2d 84, 85 (3d Cir. 1987); *Blum v. Witco Chemical Corp.*, 829 F.2d 367, 376 (3d Cir. 1987); *Saludes v. Ramos*, 744 F.2d 992, 994 (3d Cir. 1984); *Compagnie des Bauxites v. Insurance Co. of North America*, 724 F.2d 369, 371 (3d Cir. 1983), but has still recognized a need for deference to a district court judge's state law determination in some of those cases, *see, e.g., Saludes, supra*, 744 F.2d at 994 ("district judge's prediction of state law is weighty because of his or her familiarity with the particular jurisdiction"); *Compagnie des Bauxites, supra*, 724 F.2d at 371 ("[a]lthough our review is plenary, this does not mean that in discharging our function we will not take into consideration the district judge's prediction of the law in the state in which he sits").

The courts of appeals clearly are uncertain about the weight to be accorded a district court's determination of the law of the state in which it sits. This Court should grant review not only to resolve this uncertainty, but also to rule that courts of appeals must give deference to district court determinations of the law of their states and to rectify the egregious result reached in this case.

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nation, accepting that determination unless it was "clearly wrong." *See, e.g., Jablonski by Pahls v. United States*, 712 F.2d 391, 397 (9th Cir. 1983); *Monte Carlo Shirt, Inc. v. Daewoo International (America) Corp.*, 707 F.2d 1054, 1056-57 (9th Cir. 1983); *In re Mistura, Inc.*, 705 F.2d 1496, 1497 (9th Cir. 1983); *Camacho v. Civil Service Commission*, 666 F.2d 1257, 1262 (9th Cir. 1982); *Gaines v. Haughton*, 645 F.2d 761, 770 (9th Cir. 1981), *cert. denied*, 454 U.S. 1145 (1982).

II. CERTIORARI SHOULD BE GRANTED IN ORDER TO END THE CONFUSION IN THE FEDERAL COURTS SITTING IN DIVERSITY ABOUT HOW TO DETERMINE STATE LAW AS MANDATED BY *ERIE RAILROAD v. TOMPKINS*.

A. This Case Evidences a Fundamental Confusion in the Federal Courts Regarding the Effect of Lower State Court Decisions on Federal Courts Sitting in Diversity.

It is patent that the court of appeals misapplied Delaware law on the negligence issue. Of more serious concern to this Court, however, is that that misapplication grew out of a fundamental confusion regarding the effect of lower state court decisions under *Erie*. This Court should grant review to end this confusion.

On the issue of whether Nemours could recover in tort for the economic losses indisputably caused by Pierce's misconduct, the court of appeals apparently felt bound by a single lower state court ruling handed down eighteen years ago that required privity before purely economic losses could be recovered for negligence. While acknowledging that "[o]ur role in this case is predictive," and that "decisions of intermediate state courts . . . are not conclusive," (A20), the court of appeals nevertheless elevated an outdated lower state court ruling over more recent decisions of Delaware's highest court which indicated that that court would be unlikely to follow the lower court's decision, and, bolstered by an inapplicable federal admiralty case, reversed the rulings of the three Delaware district court judges sitting below, thus stripping Nemours of a jury award achieved after many months of trial.

The highest court of Delaware has given every indication that it would allow recovery in tort for economic loss regardless of privity. In *Martin v. Ryder Truck Rental, Inc.*, 353 A.2d 581 (Del. 1976), the Supreme Court of Delaware abol-

ished the common law privity requirement in products liability cases, thereby overruling the Delaware cases that had erected a bar, based on lack of privity, to products liability suits. *See, e.g., Ciociola v. Delaware Coca-Cola Bottling Co.*, 172 A.2d 252, 256-57 (Del. 1961).

In *Seiler v. Levitz Furniture Co.*, 367 A.2d 999 (Del. 1976), the same court held that a tenant of a shopping center could recover in negligence against the shopping center's architect for design defects that resulted in flood damage to the tenant's store. The Delaware high court stated: "as to privity, the case against [the architect] was tried on a negligence basis (not on a contract theory) and, to the extent [the architect] relies on the absence of privity in product liability cases, the argument is without merit in light of our recent decision in *Martin*." 367 A.2d at 1007 (citation omitted).

From these cases, Judge Stapleton, a former Delaware lawyer sitting as a Delaware district court judge in this case, determined that "the Delaware Supreme Court in *Seiler*, by relying on *Martin*, was likewise indicating an intent to abandon privity as a prerequisite to bringing suit on a negligence theory to recover financial losses suffered in the construction context." 606 F. Supp. at 1005. Thus, Judge Stapleton concluded that the Supreme Court of Delaware would permit recovery in tort for economic loss absent privity of contract.

Not only did the court of appeals disregard Judge Stapleton's considered state law determination, on which the two other Delaware district judges in this case had agreed, but it also failed to give proper regard to this controlling body of Delaware law. It ignored *Martin* completely. It stated that *Seiler* was inapplicable because the *Seiler* court had held, expressly as an alternative to its ruling on the negligence issue, that the architect was also liable to the tenant under third party beneficiary principles.

Instead, the court of appeals relied upon a single, out-

dated lower state court decision, *Crowell Corp. v. Topkis Construction Co.*, 280 A.2d 730 (Del. Super. 1971). In *Crowell*, the Superior Court of Delaware, sitting as a trial court, prohibited recovery in tort for economic loss absent privity. Not only was *Crowell* decided without the benefit of the Delaware Supreme Court's later and patently contrary holdings in *Martin* and *Seiler*, but also it was decided at a time when the privity requirement was firmly established in Delaware law. *See Ciociola, supra*, 172 A.2d at 256-57. The *Crowell* court simply was not free to depart from the *Ciociola* privity requirement, as the court itself reluctantly recognized. *See Crowell*, 280 A.2d at 731 ("[f]rom a social viewpoint there is much to be said in favor of the approach taken by plaintiff but the case law does not support plaintiff's position"). Significantly, *Crowell* has been cited by Delaware courts in only one case in the eighteen years since it was decided.[6]

The court of appeals sought to bolster its holding by noting "significant developments in the law on this issue since the date of [Judge Stapleton's decision]" (A19-A20). But the only developments cited, *East River Steamship Corp. v. Transamerica Delaval, Inc.*, 476 U.S. 858 (1986), *a federal admiralty case*, and *Aloe Coal Co. v. Clark Equipment Co.*, 816 F.2d 110 (3d Cir.), *cert. denied*, 108 S.Ct. 156 (1987), a diversity case predicting *Pennsylvania* law, have absolutely no rele-

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6. In *Oliver B. Cannon & Sons, Inc. v. Dorr-Oliver Inc.*, 312 A.2d 322 (Del. Super. 1973), the Superior Court of Delaware permitted an owner to sue a subcontractor for negligent workmanship regardless of privity of contract. The court distinguished *Crowell* on the ground that the case before it involved physical injury to property and the subsequently incurred costs of repair and replacement, *id.* at 329 -- precisely the type of damages proven by Nemours in this case. The Supreme Court of Delaware, affirming the final order in the case, held that the owner was a third party beneficiary of the subcontract. *Oliver B. Cannon & Son, Inc. v. Dorr-Oliver, Inc.*, 336 A.2d 211, 215-16 (Del. 1975). On the negligence issue, the court noted that: "[t]he decision as to [the owner's] status and its privity of contract obviates the need to consider arguments of the parties relating to *Crowell*. . . . On remand the parties are free to argue a tortious basis for damages in any way that is not inconsistent with this opinion." *Id.* at 216 n.6 (citation omitted).

vance to the determination of Delaware law. In effect, the two-judge majority has resuscitated federal common law, the very approach repudiated by *Erie Railroad v. Tompkins*, 304 U.S. 64 (1938).

The court of appeals' approach is but the most recent evidence of a fundamental disorder in the federal courts regarding the effect of lower state court decisions on federal courts sitting in diversity.

This Court in *Erie* held that the Rules of Decision Act, now codified at 28 U.S.C. § 1652, required federal courts sitting in diversity to apply not only state statutes, but also state common law. Under *Erie*, federal courts sitting in diversity have been obliged to apply state law, whether that law "shall be declared by its Legislature in a statute *or by its highest court* in a decision." 304 U.S. at 78 (emphasis added).

Erie and its progeny also made clear that if the highest court of a state is silent on a particular issue, the federal courts must predict what the highest court of a state would do. *See Commissioner v. Estate of Bosch*, 387 U.S. 456, 465 (1967); *Fidelity Union Trust Co. v. Field*, 311 U.S. 169, 177 (1940).[7]

The problem that has arisen, however, is what a federal court's responsibility is when the highest state court has not spoken directly on an issue, but there exist lower state court decisions on point. On this issue, this Court unfortunately has given mixed messages and the circuits are hopelessly confused and inconsistent.

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7. One federal appellate court judge, discussing the "unenviable task" of a federal court sitting in diversity when the highest court of a state is silent, has remarked that "[o]n occasions such as these, trial judges are asked to be omniscient in a way that is not possible for mortals." *Santiago v. Johnson Machine & Press Corp.*, 834 F.2d 84, 84 (3d Cir. 1987) (Higginbotham, J.).

A series of decisions in the 1940's held that, in the absence of clear direction from the state's highest court, the decisions of lower state courts are binding on federal courts sitting in diversity. *See Stoner v. New York Life Insurance Co.*, 311 U.S. 464, 467 (1940); *West v. American Telephone & Telegraph Co.*, 311 U.S. 223, 237 (1940); *Six Cos. v. Joint Highway District No. 13*, 311 U.S. 180, 188 (1940); *Fidelity Union Trust Co. v. Field, supra*, 311 U.S. at 177-78; *see generally* Note, *Binding Effect of Intermediate State Court Decisions on Federal Courts*, 9 Geo. Wash. L. Rev. 458 (1941).[8]

After the *Field* era, the task seemed easy enough for federal courts sitting in diversity: if the highest court of the state was silent, but a lower state court had spoken, federal courts were bound to follow the lower state court, even though the highest court of the state would be free to do otherwise.

However, the two Supreme Court opinions since the 1940's dealing with the effect to be given lower state court decisions when the highest court of a state has not spoken took away the certainty on the issue. In *King v. Order of United Commercial Travelers of America*, 333 U.S. 153, 160-61 (1948), the Court held that a decision of a lower state court was entitled to "some weight" but was "not controlling" on federal courts. And in *Commissioner v. Estate of Bosch*, 387 U.S. 456, 465 (1967), relying, *inter alia*, on *King* and over a strong dissent founded on the *Field* doctrine, the Court stated that:

> [U]nder some conditions, federal [courts] may not be

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8. In *Field*, which is perhaps the most striking example of this line of cases, the Court stated that:

> An intermediate state court in declaring and applying the state law is acting as an organ of the State and its determination, in the absence of more convincing evidence of what the state law is, should be followed by a federal court in deciding a state question.

Field, 311 U.S. at 177-78.

> bound even by an intermediate state appellate court ruling. It follows here then, that when the application of a federal statute is involved, the decision of a state trial court as to an underlying issue of state law should *a fortiori* not be controlling. . . . If there be no decision by [the highest court of the state] then federal [courts] must apply what they find to be the state law after giving "proper regard" to relevant rulings of other courts of the State.

The effect of *King* and *Bosch* was to leave the federal courts sitting in diversity without clear direction regarding the effect to be given lower state court rulings. Nevertheless, this Court has not directly addressed the issue of the effect of lower state court decisions since *Bosch*. The result has been that courts of appeals have taken inconsistent and widely varying approaches.

Some courts of appeals, for example, consider themselves absolutely bound by lower state court decisions. Thus, the court in *Birmingham Fire Insurance Co. v. Winegardner & Hammons, Inc.*, 714 F.2d 548, 550 (5th Cir. 1983) (emphasis in original), stated that, "when the supreme court of a state has not spoken to a particular issue, the well-established practice of this Circuit is to follow the opinion of the highest court which *has* written on the matter." *See also Burrus v. Young*, 808 F.2d 578, 581 (7th Cir. 1986); *Studstill v. Borg Warner Leasing*, 806 F.2d 1005, 1007 (11th Cir. 1986); *Hill v. Bache Halsey Stuart Shields Inc.*, 790 F.2d 817, 827 (10th Cir. 1986); *Allen v. A. G. Edwards & Sons, Inc.*, 606 F.2d 84, 87 (5th Cir. 1979); *Farmer v. Travelers Indemnity Co.*, 539 F.2d 562, 563 (5th Cir. 1976); *Continental Grain Co. v. Martin*, 536 F.2d 592, 593 (5th Cir.), *cert. denied*, 429 U.S. 1024 (1976).

Other courts of appeals, reflecting this Court's direction in *Field*, follow the rule that they are bound by lower state court decisions, "unless . . . convinced by other persuasive data that the highest court of the state would decide otherwise." *Kochins v. Linden-Alimak, Inc.*, 799 F.2d 1128, 1140

(6th Cir. 1986). *See, e.g., Miller v. Fairchild Industries, Inc.*, 797 F.2d 727, 735 (9th Cir. 1986); *Provau v. State Farm Mutual Automobile Insurance Co.*, 772 F.2d 817, 820 (11th Cir. 1985); *McCoy v. Richards*, 771 F.2d 1108, 1110 (7th Cir. 1985); *O'Neil v. Great Plains Women's Clinic, Inc.*, 759 F.2d 787, 790 (10th Cir. 1985); *Flintkote Co. v. Dravo Corp.*, 678 F.2d 942, 945 (11th Cir. 1982); *Delano v. Kitch*, 663 F.2d 990, 996 (10th Cir. 1981), *cert. denied*, 456 U.S. 946 (1982).

A third group of courts of appeals regard lower state court rulings as somewhat less important in ascertaining state law. *See, e.g., General Electric Credit Corp. v. Ger-Beck Machine Co.*, 806 F.2d 1207, 1209 (3d Cir. 1986) ("significant weight"); *Sarnoff v. American Home Products Corp.*, 798 F.2d 1075, 1084 (7th Cir. 1986) ("significant evidence"); *Ciccarelli v. Carey Canadian Mines, Ltd.*, 757 F.2d 548, 553 n.3 (3d Cir. 1985) ("federal court must consider and give due regard"); *Mathis v. Eli Lilly & Co.*, 719 F.2d 134, 141 n.15 (6th Cir. 1983) ("datum not to be disregarded by the federal court"); *Coleman v. Western Electric Co.*, 671 F.2d 980, 983 (6th Cir. 1982) ("an *Erie* indicator"); *see also Dale Baker Oldsmobile, Inc. v. Fiat Motors of North America*, 794 F.2d 213, 218 (6th Cir. 1986).

The confusion in the courts of appeals on this important issue is attributable to this Court's uneven direction. That confusion created a climate in which the court of appeals in this case felt free to elevate an outdated lower state court ruling over the more recent teachings of the state's highest court. This unpredictability and conflict among circuits can be corrected only by clear direction from this Court whose seemingly contradictory decisions are the basis for these conflicts. For these reasons, this Court should grant review here.

B. This Case Evidences a Fundamental Confusion in the Federal Courts Regarding Whether Decisions of a State's Highest Court Are Binding on Federal Courts Sitting in Diversity.

Whatever its effect on lower state court decisions, *Erie*

seemed to make clear that the decisions of the *highest* courts of the states are binding on federal courts sitting in diversity. In this case, however, the panel majority disregarded the decisions of the highest court of Delaware on the third party beneficiary issue, suggesting the danger that the clarity of *Erie* may be being diluted by the passage of time.

The highest court of Delaware has firmly established that the intent to confer third party beneficiary status is to be determined from the language of the contract, and only from the language of the contract. *See Oliver B. Cannon & Son, Inc. v. Dorr-Oliver, Inc.*, 336 A.2d 211, 215 (Del. 1975); *Royal Indemnity Co. v. Alexander Industries, Inc.*, 211 A.2d 919, 920 (Del. 1965); *see also Sears, Roebuck & Co. v. Jardel Co.*, 421 F.2d 1048, 1054 (3d Cir. 1970) (applying Pennsylvania law, but cited with approval in *Cannon*).

Acknowledging this requirement under Delaware law, the panel majority nonetheless relied on a host of factors external to the contract, offering as support for its approach, unprecedented under Delaware law, only its belief that "[t]he language of a contract . . . cannot be divorced from the context in which it was written" (A10). It was the majority's unauthorized examination of that "context"—including the nature of the construction industry, a letter from Nemours to Gilbane, the language of the Pierce/Federal performance bond, the pattern of the litigation itself, and provisions in the Nemours/Gilbane general contract—that led it to conclude that "the subcontract does not manifest an intent by Pierce and Gilbane to confer third party beneficiary status on Nemours" (A18).

As Judge Sloviter's dissent noted, had the panel majority followed the rulings of Delaware's highest court, it would have found "sufficient evidence under Delaware law . . . that Gilbane and Pierce intended to make Nemours a beneficiary of the subcontract" (A40). Indeed, had the panel majority taken as its frame of reference the state cases on point, such

as *Cannon*, it would have found that the precise indicia of intent to create third party beneficiary status identified as significant in those cases also appeared in the Gilbane/Pierce subcontract—as the Delaware district judges who reviewed and applied Delaware law on this issue had determined.[9]

Rather than rely on *Cannon*, however, the panel majority sought to distinguish it, and did so in a single paragraph, in disarmingly conclusory terms: "What distinguishes the present case from *Cannon* is Pierce's and Gilbane's expressed intent that there be no third party beneficiary relationship between Pierce and Nemours" (A17). Because, however, the majority divined that "intent" from sources external to the language of the subcontract itself, the alleged distinction is meaningless under Delaware law.

The panel majority's disregard of decisions of the highest court of Delaware reflects the uncertainty that has developed in the fifty-one years of *Erie* jurisprudence on the issue of whether and to what degree decisions of a state's highest court are binding on federal courts sitting in diversity. It seems likely that the panel majority felt free to avoid the Delaware Supreme Court's decision in Cannon because this Court has suggested on at least two occasions, albeit in dicta, that some circumstances may exist in which decisions of a state's highest court may not be controlling on federal courts sitting in diversity. Even so, why the panel majority would employ this occasion to deprive a non-profit children's hospital of a $29 million jury verdict is, at the very least, puzzling.

The Court first suggested that the *Erie* rule might not be

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9. For example, in *Cannon*, a case holding that the owner was the third party beneficiary of the subcontract between the general contractor and the subcontractor, the highest court of Delaware emphasized that the subcontract identified the owner (as in the Gilbane/Pierce subcontract); contained an indemnification clause whereby the subcontractor would indemnify the owner against certain losses (as in the Gilbane/Pierce subcontract); and contained a warranty clause running from the subcontractor to the owner (as in the Gilbane/Pierce subcontract). 336 A.2d at 215.

absolute in *Meredith v. City of Winter Haven*, 320 U.S. 228, 234 (1943): "the rulings of the Supreme Court of Florida . . . must be taken as controlling here unless it can be said with some assurance that the Florida Supreme Court will not follow them in the future . . . ." Similarly, in *Bernhardt v. Polygraphic Co. of America*, 350 U.S. 198, 205 (1956), the Court held that a 1910 decision of the highest court of Vermont was controlling, but qualified its holding by adding: "there appears to be no confusion in the Vermont decisions, no developing line of authorities that casts a shadow over the established ones, no dicta, doubts or ambiguities in the opinions of Vermont judges on the question, no legislative development that promises to undermine the judicial rule."

The uneven direction by the Court on this issue has led some courts of appeals to depart sporadically from the decisions of the highest court of the state whose law they are applying. *See, e.g., Miller v. Premier Corp.*, 608 F.2d 973, 985-87 (4th Cir. 1979); *Mason v. American Emery Wheel Works*, 241 F.2d 906, 909-10 (1st Cir.), *cert. denied*, 355 U.S. 815 (1957); *see also Roginsky v. Richardson-Merrell, Inc.*, 378 F.2d 832, 851 (2d Cir. 1967). Other courts have considered themselves absolutely bound by *Erie* to apply the decisions of the highest court of the state, regardless of the circumstances. *See, e.g., Ciccarelli v. Carey Canadian Mines, Ltd.*, 757 F.2d 548, 553 n.3 (3d Cir. 1985); *Birmingham Fire Insurance Co. v. Winegardner & Hammons*, 714 F.2d 548, 551 (5th Cir. 1983); *see also Rhynes v. Branick Manufacturing Corp.*, 629 F.2d 409, 410 (5th Cir. 1980) ("[i]n matters of Texas substantive law, our relationship to the Texas Supreme Court is all but identical to that of a Texas intermediate appellate court").

This Court should grant review because the uneven direction on the issue of the binding effect of decisions of the highest court of a state has led to uncertainty among the courts of appeals. In this case, it is clear that on the third party beneficiary issue, as on the negligence issue, the panel majority simply substituted its own view of what Delaware

law should be for what Delaware law actually is. It is the lack of direction from this Court that created the climate in which the majority felt free to do so.

CONCLUSION

This case represents a serious deviation from *Erie*. The panel majority of the court of appeals gave no weight to the district court's determinations of state law, made independently by three highly regarded Delaware judges. Moreover, the court of appeals on one issue elevated the holding of an outdated lower court case over more recent decisions by the highest court of the state that evidenced a different view, and, on the other, completely disregarded precedent from the highest court of the state. Rendered in an atmosphere of confusion about the role of a district court's state law determinations and about whether or not lower state court decisions or even the decisions of the highest courts of the states are in fact binding on federal courts sitting in diversity, this ruling calls out for review.

Respectfully submitted,

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